Report

of the

Examination of

Fountain City Mutual Insurance Company

Fountain City, Wisconsin

As of December 31, 2004

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State of Wisconsin / OFFICE OF THE COMMISSIONER OF INSURANCE

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May 13, 2005

Honorable Jorge Gomez
Commissioner of Insurance
State of Wisconsin
125 South Webster Street
Madison, Wisconsin 53702

Commissioner:

In accordance with your instructions, an examination has been performed as of December 31, 2004, of the affairs and financial condition of:

FOUNTAIN CITY MUTUAL INSURANCE COMPANY
Fountain City, Wisconsin

and the following report thereon is respectfully submitted:

I. INTRODUCTION

The previous examination of Fountain City Mutual Insurance Company (the company) was made in 2000 as of December 31, 1999. The current examination covered the intervening time period ending December 31, 2004, and included a review of such subsequent transactions deemed essential to complete this examination.

The “Summary of Examination Results” contains elaboration on all areas of the company's operations. Special attention was given to the action taken by the company to satisfy the recommendations and comments made in the previous examination report.

The company was organized as a town mutual insurance company on May 16, 1874, under the provisions of the then existing Wisconsin Statutes. The original name of the company was the Fountain City Mutual Farmers Fire Insurance Company. Subsequent amendments to the company's articles and bylaws changed the company's name to that presently used.

During the period under examination, there were no amendments to the articles of incorporation and no amendments to the bylaws.

The company is currently licensed to write property, including windstorm and hail and nonproperty insurance. The company is currently licensed to write business in the following counties:

Buffalo	Dunn
Eau Claire	Pepin
Pierce	Trempealeau

A review was made of the policy and application forms currently used by the company. The company issues approved policies with or without endorsements for terms of one year with premiums payable on the advance premium basis. The company also charges a policy fee equal to $25 for payments of premium after the due date.

Business of the company is acquired through 18 agents, three of whom are directors of the company. Agents are presently compensated for their services as follows:

Type of Policy	Compensation
All Policies	12%

Agents have authority to adjust losses up to $1,000; but, in practice, the company does not currently have any agents adjusting losses. Losses are currently adjusted by Laverne Syens, manager of the company. Adjusters receive $50.00 for each loss adjusted plus $0.405 per mile for travel allowance.

Policyholders may participate in the management and control of the company by attending and voting at all annual or special meetings of the members. No member may vote by proxy. The annual meeting of the company for the election of directors and special meetings of the company are held in accordance with its articles of incorporation.

Board of Directors

The board of directors consists of nine members divided into three classes. One class is elected at each annual meeting for a term of three years. Vacancies on the board may be filled by the directors on an interim basis until the next annual meeting when a director shall be chosen for the unexpired term.

The current board of directors consists of the following policyholders of the company:

Name	Principal Occupation	Residence	Expiry
Lee Weiland*	President – Fountain City Mutual Insurance Company	Arcadia	2006
Paul Rosenow	Vice President – Fountain City Mutual Insurance Company	Cochrane	2007
Laverne Syens*	Secretary & Treasurer – Fountain City Mutual Insurance Company	Stevens Point	2008
Joseph Greshik	Farmer	Cochrane	2006
Jeremy Anderson	Farmer	Alma	2007
Gary Bond	Retired Bus Driver	Fountain City	2008
Mark Schultz	Farmer & Inspector	Alma	2006
Dale Mann*	Retired Insurance Agent	Fountain City	2007
William Wiess Jr.	Realtor	Mondovi	2008

Directors who are also agents are identified with an asterisk.

Members of the board currently receive $75.00 for each meeting attended and $0.405 per mile for travel expenses.

Officers

Officers are elected by the board of directors from among its members and hold office for one year or until their successors are duly elected and qualified. Officers serving at the present time are as follows:

Name	Office	2004 Salary
Lee Weiland	President	$ 300
Paul Rosenow	Vice President	0
Laverne Syens	Secretary &Treasurer	0
Laverne Syens	Manager	72,477*

* Also includes his independent contractor salary, prior to his appointment as manager in February 2004.

Committees of the Board

The company's bylaws allow for the formation of certain committees by the board of directors. The committees at the time of the examination are listed below:

Adjusting Committee
Laverne Syens, Chair
Lee Weiland
Mark Schultz

Executive/Investment Committee
Paul Rosenow, Chair
Joseph Greshik
Mark Schultz
Laverne Syens

Growth of Company

The growth of the company since the previous examination as compiled from its filed annual statements was as follows:

Year	Net Premiums Earned	Policies In Force	Net Income	Admitted Assets	Policyholders' Surplus
2004	$692,612	1,403	$ 158,911	$1,466,691	$785,512
2003	547,102	1,531	119,765	1,093,053	408,184
2002	512,081	1,551	(115,929)	1,125,527	336,598
2001	546,222	1,456	(266,197)	1,180,671	559,993
2000	396,802	1,474	90,740	1,417,384	862,669
1999	486,602	1,540	(54,840)	1,162,215	674,343

The ratios of gross and net premiums written to surplus as regards policyholders since the previous examination were as follows:

Year	Gross Premiums Written	Net Premiums Written	Ending Surplus	Writings Ratios Net	Writings Ratios Gross
2004	$1,197,860	$720,386	$785,512	92%	152%
2003	1,126,137	546,506	408,184	134	276
2002	1,176,003	565,337	336,598	168	349
2001	1,048,835	636,153	559,993	114	187
2000	1,031,337	351,814	862,669	41	120
1999	1,062,962	514,071	674,343	76	207

For the same period, the company's operating ratios were as follows:

Year	Net Losses and LAE Incurred	Other Underwriting Expenses Incurred	Net Earned Premiums	Loss Ratio	Expense Ratio	Com-posite Ratio
2004	$295,646	$320,333	$692,612	43%	44%	87%
2003	175,847	329,610	547,102	32	60	92
2002	369,934	263,979	512,081	72	47	119
2001	571,657	267,163	546,222	105	42	147
2000	165,714	162,357	396,802	42	46	88
1999	362,491	201,342	486,602	74	39	114

Surplus, admitted assets, and net premiums earned increased 14.2%, 26.2%, and 42.3%, respectively, over the examination period. Surplus increased between 1999 and 2000 and then decreased in 2001 and 2002 due to years with high net losses and LAE incurred resulting in net losses of $(266,197) in 2001 and $(115,929) in 2002. The company strengthened its underwriting standards and the number of policies in force decreased to 1,403 at year-end 2004.

The company’s composite ratio is 87% in 2004, the lowest of the examination period and the company had a net income of $158,911 in 2004, the highest of the examination period.

II. REINSURANCE

The examiners' review of the company's reinsurance portfolio revealed there is currently one ceding treaty. The treaty contained a proper insolvency clause and complied with s. Ins 13.09 (3), Wis. Adm. Code, concerning maximum wind loss. Company retentions of risk complied with s. Ins 13.06, Wis. Adm. Code.

Reinsurer:	Wisconsin Reinsurance Corporation (WRC)
Effective date:	January 1, 2005
Termination provisions:	Either party may terminate the contract as of any subsequent January 1 by giving to the other party at least 90 days notice in writing.
1. Type of contract:	Class A Excess of Loss
Lines reinsured:	All liability (nonproperty) business
Company's retention:	Excess of Loss: $10,000 in respect to each and every loss occurrence. Aggregate Stop Loss: 60% of the company’s net liability premiums subject to a minimum retention of $60,000.
Coverage:	Excess of Loss Reinsurer shall be liable for 100% of each and every loss occurring on the business covered, in excess of the company’s net retention, subject to the following maximum policy limits: • $1,000,000 per occurrence, single limit, combined for bodily injury and property damage liability. • $1,000,000 split limits, in any combination of bodily injury and property liability. • $5,000 for medical payments, per person; $25,000 per accident. Aggregate Stop Loss Reinsurer shall indemnify the company for 100% of net losses in excess of 60% of the company’s net casualty premiums written.
Reinsurance premium:	For each annual period this contract is in effect, the company shall pay to the reinsurer 40% of the premium written for each and every policy issued with respect to business covered.
Ceding commission:	None

2. Type of contract: Class B First Surplus

Lines reinsured: All property business

Company's retention: $400,000 in respect to each risk

Coverage: When the company's net retention is $400,000 or more in respect to a risk, the company may cede on a pro rata basis, and the reinsurer shall be obliged to accept up to $800,000. When the company's net retention is $400,000 or less in respect to a risk, the company may cede on a pro rata basis, and the reinsurer shall be obligated to accept up to 50% of such risk.

Reinsurance premium: The pro rata portion of all premiums, fees and assessments charged by the company corresponding to the amount of each risk ceded.

Ceding commission: 15% of the premium paid to reinsurer under this contract.

Contingent commission:
15% of the net profit accruing to the reinsurer during each accounting period. Net profit is defined as follows:

- Premium earned for the accounting period; less
- Ceding commission on premium earned for the period; less
- Expenses incurred by the reinsurer calculated at 10% of premium earned; less
- Losses and LAE incurred for the period; less
- The reinsurer's net loss from the immediately preceding accounting period.

3. Type of contract: Class C-1 First Layer Excess of Loss Reinsurance

Lines reinsured: All property business

Company's retention: $40,000 in respect to each and every risk resulting from one loss occurrence.

Coverage: 100% of any loss, including loss adjustment expense, in excess of $40,000 in respect to each and every risk resulting from one loss occurrence. The reinsurer's limit of liability shall be $60,000 in respect to each and every loss occurrence.

Reinsurance premium: The rate in effect shall be determined by taking the sum of the four years' losses incurred (paid plus outstanding) by the reinsurer divided by the total of the net premiums written for the same period, multiplied by the factor 100/80ths. Subject to a minimum rate of 6% and a maximum rate of 22%

The current year's rate is 6% of net premium written. Annual deposit premium of $75,900 payable in equal

		monthly installments of $6,325 each. The minimum premium for the current year is $60,000.
	Ceding commission:	None
4.	Type of contract:	Class C-2 Second Layer Excess Of Loss Reinsurance
	Lines reinsured:	All property business
	Company's retention:	$100,000 in respect to each and every risk resulting from one loss occurrence
	Coverage:	100% of any loss, including loss adjustment expense, in excess of $100,000 in respect to each and every risk resulting from one loss occurrence. The reinsurer's limit of liability shall be $300,000 in respect to each and every loss occurrence.
	Reinsurance premium:	3.5% of net premiums in respect to business covered. An annual deposit premium of $44,275 payable in equal monthly installments of $3,690 each. The minimum premium for the current year is $35,000.
	Ceding commission:	None
5.	Type of contract:	Class D/E-1 First Layer Aggregate Property Stop Loss Reinsurance
	Lines reinsured:	All property business
	Company's retention:	The company shall retain net for its own account an amount of net losses, including loss adjusting expenses, equal to not less than 70% of the company's net premium written, subject to a minimum retention of $600,000.
	Coverage:	100% of the amount, if any, by which the aggregate of the company's net losses, including loss adjusting expenses, exceed an amount equal to 70% of the company's net premiums written.
	Reinsurance premium:	The rate in effect shall be determined by taking the sum of the eight year's losses incurred by the reinsurer divided by the total of the net premiums written for the same period multiplied by the factor of 100/80ths. Subject to a minimum rate of 6% and a maximum rate of 25% of current net written premiums. The rate for current annual period is 15%. An annual deposit premium of $189,750 payable in equal monthly installments of $15,813 each. Minimum premium for the current year is $150,000.
Ceding commission:		None

III. FINANCIAL DATA

The following financial statements reflect the financial condition of the company as reported to the Commissioner of Insurance in the December 31, 2004, annual statement. Adjustments made as a result of the examination are noted at the end of this section in the area captioned "Reconciliation of Policyholders' Surplus."

Fountain City Mutual Insurance Company
Statement of Assets and Liabilities
As of December 31, 2004

Assets

Assets	Ledger	Nonledger	Not Admitted	Net Admitted
Cash in company's office	$ 100	$ 0	$ 0	$ 100
Cash deposited in checking account	108,020			108,020
Cash deposited at interest	430,649			430,649
Bonds	149,493			149,493
Stocks and mutual fund investments	513,196			513,196
Real estate	59,630			59,630
Premiums, agents' balances and installments:				
In course of collection	3,812			3,812
Deferred and not yet due	179,215			179,215
Investment income accrued		4,747		4,747
Electronic data processing equipment	8,790			8,790
Other expense-related assets:				
Commission Due Reinsurer	9,039			9,039
Furniture and fixtures	220		220	
Totals	$1,462,164	$4,747	$220	$1,466,691

Liabilities and Surplus

Net unpaid losses	$ 64,925
Unpaid loss adjustment expenses	2,619
Commissions payable	27,532
Fire department dues payable	1,757
Federal income taxes payable	1,329
Unearned premiums	481,277
Reinsurance payable	73,470
Amounts withheld for the account of others	5,614
Payroll taxes payable (employer’s portion)	1,374
Other liabilities:	
Expense related:	
Accounts payable	2,191
Nonexpense related:	
Premiums received in advance	19,091
Total Liabilities	681,179
Policyholders' surplus	785,512
Total Liabilities and Surplus	$1,466,691

Fountain City Mutual Insurance Company
Statement of Operations
For the Year 2004

Net premiums and assessments earned		$692,612
Deduct:		
Net losses incurred	$266,066	
Net loss adjustment expenses incurred	29,580	
Other underwriting expenses incurred	320,333	
Total losses and expenses incurred		615,979
Net underwriting gain (loss)		76,633
Net investment income:		
Net investment income earned	2,522	
Net realized capital gains	(470)	
Total investment gain (loss)		2,052
Other income (expense):		
Administrative Fees	84,185	
Other Income	71	
Total other income		84,256
Net income (loss) before federal income taxes		162,941
Federal income taxes incurred		4,030
Net Income (Loss)		$158,911

Fountain City Mutual Insurance Company
Reconciliation and Analysis of Surplus as Regards Policyholders
For the 5-Year Period Ending December 31, 2004

The following schedule is a reconciliation of surplus as regards policyholders during the period under examination as reported by the company in its filed annual statements:

	2004	2003	2002	2001	2000
Surplus, beginning of year	$408,184	$336,598	$559,993	$862,669	$674,343
Net income	158,911	119,765	(115,929)	(266,197)	90,740
Net unrealized capital gains or (losses)	217,797	(52,381)	(104,829)	(35,868)	96,837
Change in nonadmitted assets	620	4,202	(2,637)	(611)	749
Surplus, end of year	$785,512	$408,184	$336,598	$559,993	$862,669

Reconciliation of Policyholders' Surplus

The examination resulted in no adjustments to policyholders' surplus. The amount reported by the company as of December 31, 2004, is accepted.

IV. SUMMARY OF EXAMINATION RESULTS

Compliance with Prior Examination Report Recommendations

Comments and recommendations contained in the last examination report and the action taken on them by the company are as follows:

1. Fidelity Bond and Other Insurance—It is recommended that the company obtain proper fidelity bond coverage for all employees in accordance with s. 13.05 (6), Wis. Adm. Code.

   Action—Compliance

2. Disaster Recover Plan—It is recommended that the company develop a written disaster recovery plan.

   Action—Compliance

3. Net Unpaid Losses—It is recommended that the company establish an IBNR reserve for the extended coverage and nonproperty losses on Schedule J-1 of the annual statement.

   Action—Compliance

4. Unpaid Loss Adjustment Expense—It is recommended that the company estimate the expenses necessary to adjust unpaid losses using a paid to paid methodology.

   Action—Compliance

Current Examination Results

Corporate Records

The minutes of the annual meetings of policyholders and meetings of the board of directors and committees thereof were reviewed for the period under examination and also for the subsequent period.

Biographical data relating to company officers and directors have not been reported in accordance with the provisions of s. Ins 6.52, Wis. Adm. Code. It was noted during the examination that biographical data relating to one new officer and one new director in 2004 have not been reported to this office. It is recommended that the company report biographical data relating to all new officers and directors in accordance with s. Ins 6.52, Wis. Adm. Code.

The company has executed formal written agreements with its agents. The contracts include language indicating the agent will represent the company's interests "in good faith."

Conflict of Interest

In accordance with a directive of the Commissioner of Insurance, each company is required to establish a procedure for the disclosure to its board of directors of any material interest or affiliation on the part of its officers, directors, or key employees which conflicts or is likely to conflict with the official duties of such person. A part of this procedure is the annual completion of a conflict of interest questionnaire by the appropriate persons. The company has adopted such a procedure for disclosing potential conflicts of interest. Conflict of interest questionnaires were reviewed for the period under examination with apparent conflicts being noted. Paul Rosenow, Vice President, is also a chairman of the board of directors of Waumandee State Bank. It was noted during review of the board minutes that he does not abstain from voting on investment matters involving Waumandee State Bank. It is recommended that the directors with conflicts of interest properly abstain from voting on matters involving their interest and the minutes clearly indicate such abstentions pursuant to s. 612.18, Wis. Stat.

Fidelity Bond and Other Insurance

The company is afforded coverage under the terms of the following bonds or contracts and has complied with s. Ins 13.05 (6), Wis. Adm. Code, which sets forth the minimum requirements for fidelity bond coverage:

Type of Coverage	Coverage Limits
Fidelity bond	$ 100,000
Combined professional liability and officers and directors liability	500,000
Worker's compensation:	
Employee injury	Statutory
Employee liability:	
Each accident	500,000
Each employee	500,000
Policy limit	500,000
Business owners	
Liability and medical expenses	1,000,000
Medical expenses—each person	5,000
Tenant fire legal	50,000
Hired auto and non-owned auto liability	1,000,000

Underwriting

The company has a written underwriting guide. The guide covers all the lines of business that the company is presently writing.

The company has a formal inspection procedure for both new and renewal business. All new applications and renewal business are inspected by committee members who are independent of the risk under consideration and review.

Claims Adjusting

The company has an adjusting committee consisting of at least three directors as required by s. 612.13 (4), Wis. Stat. The function of this committee is to adjust or supervise the adjustment of losses.

Accounts and Records

The examiners' review of the company's records indicated that the company is in compliance with s. Ins 13.05, Wis. Adm. Code, which sets forth the minimum standards for the handling of cash and recording of cash transactions by town mutual insurance companies. The examiners noted the following:

1. A proper policy register is maintained
2. A proper cash receipts journal is maintained
3. A proper cash disbursements journal is maintained
4. A proper general journal is maintained
5. A proper general ledger is maintained

An extensive review was made of income and disbursement items. Cash receipts were traced from source records and the proper recording and eventual deposit thereof ascertained. Negotiated checks issued during the period under examination were reviewed, test checked for proper endorsement, and traced to cash records. The verification of assets and determination of liabilities were made as of December 31, 2004.

The company is audited annually by an outside public accounting firm.

EDP Environment

Company personnel were interviewed with respect to the company's electronic data processing environment. Access to the computers is limited to people authorized to use the computers.

Company personnel back up the computers daily and the backed-up data is kept on-site in a fireproof safe and one copy is kept off-site.

A manual which describes how to use the company's software and outlines the steps to complete specific tasks assists in the continuity of operations for seldom-used applications, training, or when staff turnover occurs. The company has manuals documenting the use of its software.

Business Continuity Plan

A business continuity plan identifies steps to be performed by a company in the event of business interruptions including, but not limited to, the inability to access its computer, the loss of information on its computer, the loss of a key employee, or the destruction of its office building. The company has developed a business continuity plan. The company's business continuity plan appears to be adequate.

Invested Assets

Section 610.23, Wis. Stat., requires insurers to hold all investments and deposits of its funds in its own name except that:

(1) Securities kept under a custodial agreement or trust arrangement with a bank or banking and trust company may be issued in the name of a nominee of the bank or banking and trust company; and

(2) Any insurer may acquire and hold securities in bearer form.

For securities not held under a custodial agreement or trust arrangement with a bank or banking and trust company, s. Ins 13.05 (4), Wis. Adm. Code, requires that:

> Non-negotiable evidences of company investments such as registered bonds, certificates of deposits, notes, etc., shall be maintained in a safe or vault with adequate safety controls or in a safety deposit box in a bank. Negotiable evidences of company investments shall be maintained in a safety deposit box in a bank. Access to a company safety deposit box containing negotiable securities shall require the presence and signature of at least 2 officers, directors or employees of the company.

The company is in compliance with these requirements.

Investment Rule Compliance

The investment rule for town mutual insurers allows a company to invest in common stocks, common stock mutual funds, and other higher risk investments (referred to as "Type 2") provided that the town mutual has a sufficient amount of lower risk investments (referred to as "Type 1"). A town mutual may invest in Type 2 securities only if it already has sufficient Type 1 investments. Type 1 investments must equal or exceed the greater of items 1, 2, or 3.

1.	Liabilities plus $300,000	$ 987,179
2.	Liabilities plus 33% of gross premiums written	1,076,474
3.	Liabilities plus 50% of net premiums written	1,041,372
4.	Amount required (greater of 1, 2, or 3)	1,076,474
5.	Amount of Type 1 investments as of 12/31/2004	625,004
6.	Excess or (deficiency)	$ (451,470)

The company does not have sufficient Type 1 investments. The company's Type 2 investments in WRC common stock and NAMICO common stock have been approved by this office and no other Type 2 investments have been made.

ASSETS

Cash and Invested Cash **$538,769**

The above asset is comprised of the following types of cash items:

Cash in company's office	$ 100
Cash deposited in banks-checking accounts	108,020
Cash deposited in banks at interest	430,649
Total	$538,769

Cash in company's office at year-end represents the company's petty cash fund. A physical count was made by the examiners during the course of the examination and the balance reconciled to year-end.

Cash deposited in banks subject to the company's check and withdrawal consists of one account maintained in a local bank. Verification of the checking account balance was made by obtaining confirmation directly from the depository and reconciling the amounts shown thereon to company records.

Cash deposited in banks represents the aggregate of 13 deposits in 10 depositories. Deposits were verified by direct correspondence with the respective depositories and the deposits held under the safekeeping agreement were confirmed by the custodian. Interest received during the year 2004 totaled $12,307 and was verified to company cash records. Rates of interest earned on cash deposits ranged from 1.00% to 7.70%. Accrued interest on cash deposits totaled $2,464 at year-end.

Book Value of Bonds **$149,493**

The above asset consists of the aggregate book value of bonds held by the company as of December 31, 2004. Bonds owned by the company are located in the custodial bank.

Bonds held under the safekeeping agreement were confirmed by the custodian. Bond purchases and sales for the period under examination were checked to brokers' invoices and advices. The company's investment in bonds was in conformance with Wisconsin Statutes and the rules of the Commissioner of Insurance as regards investments made by town mutual insurers.

Interest received during 2004 on bonds amounted to $7,339 and was traced to cash receipts records. Accrued interest of $2,283 at December 31, 2004, was checked and allowed as a nonledger asset.

Stocks and Mutual Fund Investments **$513,196**

The above asset consists of the aggregate market value of stocks held by the company as of December 31, 2004. Stocks owned by the company are located in the company's fireproof safe.

Stock certificates were physically examined by the examiners. The company did not purchase any stocks or mutual funds during the period under examination. The company's investment in stocks was in conformance with Wisconsin Statutes and the rules of the Commissioner of Insurance as regards investments made by town mutual insurers.

There were no dividends received during 2004 on the common stocks that the company owns and there were no accrued dividends at December 31, 2004.

Book Value of Real Estate **$59,630**

The above amount represents the company's investment in real estate as of December 31, 2004. The sole real estate holding is the company's office building located in Fountain City.

The required documents supporting the validity of this asset were reviewed and were in order. Adequate hazard insurance was carried on the real estate and contents as noted under the caption, "Fidelity Bond and Other Insurance." The company's investment in real estate and related items was in conformance with the Wisconsin Statutes and the rules of the Commissioner of Insurance as regards investments made by town mutual insurers. Real estate depreciation is calculated using the straight-line method.

Premiums, Agents' Balances in Course of Collection **$3,812**

This asset represents the amounts due from agents or policyholders which are not in excess of 90 days past due at year-end. A review of detailed premium records verified the accuracy of this asset.

Premiums Deferred and Not Yet Due **$179,215**

This asset represents modal premium installments (such as monthly, quarterly, etc.) that are not yet due. A review of a sample from the company's detailed list of deferred premiums verified the accuracy of this asset.

Investment Income Accrued **$4,747**

Interest due and accrued on the various assets of the company at December 31, 2004, consists of the following:

Cash deposited at interest	$2,464
Bonds	2,283
Total	$4,747

Electronic Data Processing Equipment **$8,790**

The above balance consists of computer hardware and operating system software, net of depreciation as of December 31, 2004. A review of receipts and other documentation verified the balance. Non-operating system software was properly nonadmitted.

Commission Due Reinsurer **$9,039**

The above asset represents reinsurance commissions receivable in the amount of $2,930.45 and deferred reinsurance commissions that the company expected to receive as of December 31, 2004, under its contract with Wisconsin Reinsurance Corporation. The reinsurance commission receivable was traced to subsequent receipt in 2005. A review of the terms of the reinsurance agreement and year-end accountings with the reinsurer verified the above reinsurance deferred commissions asset.

Furniture and Fixtures **$0**

This asset consists of $220 of office equipment and furniture owned by the company at December 31, 2004. In accordance with annual statement requirements, this amount has been reported as a nonadmitted asset, thus the balance shown above is $0.

LIABILITIES AND SURPLUS

Net Unpaid Losses **$64,925**

This liability represents losses incurred on or prior to December 31, 2004, that remained unpaid as of that date. The examiners reviewed the reasonableness of this liability by totaling actual loss payments made subsequent to December 31, 2004, with incurred dates in 2004 and prior years. To the actual paid loss figure was added an estimated amount for 2004 and prior losses remaining unpaid at the time of the examination. The examiners' development of unpaid losses is compared with the amount estimated by the company in the following schedule.

	Company Estimate	**Examiners' Development**	**Difference**
Incurred but unpaid losses	$253,989	$248,455	$5,534
Less: Reinsurance recoverable on unpaid losses	189,064	188,604	460
Net Unpaid Losses	$ 64,925	$ 59,851	$5,074

The above difference of $5,074 was not considered material for purposes of this examination. The difference between the developed loss reserve and the company estimate is due to the case basis loss reserves being under reserved by $3,850 and the incurred but not reported loss reserves being over reserved by $8,924.

The examiners' review of claim files included open claims, paid claims, claims closed without payment, and all claims which were denied during the examination period. The review indicated that claims are investigated and evaluated properly and that payments are made promptly and in accordance with policy provisions upon the submission of a proper proof of loss. In addition, the review of claims handling procedures and files revealed the following:

1. A proper loss register is maintained.
2. Claim files contained sufficient investigatory data and documentation to verify settlement payments or reserve estimates.
3. Proofs of loss were properly signed.

Unpaid Loss Adjustment Expenses **$2,619**

This liability represents the company's estimate of amounts necessary to settle losses which were incurred prior to December 31, 2004, but which remained unpaid as of year-end. The company establishes this liability based on a review of the claims at year-end and uses an estimate of what will be paid for adjusting expenses. A portion of the manager's salary at year-end is allocated to the unpaid LAE because he does the majority of the loss adjusting.

The examiners' analysis of expenses incurred in the current year related to the settlement of prior year losses as well as estimates of amounts necessary to settle any prior losses remaining unpaid at the examination date, determined this liability to be adequately stated.

Commissions Payable **$27,532**

This liability represents the commissions payable to agents as of December 31, 2004. The examiners reviewed the company's subsequent commission payments and found the liability to be reasonably stated.

Fire Department Dues Payable **$1,757**

This liability represents the fire department dues payable to the State of Wisconsin as of December 31, 2004.

The examiners reviewed the company's fire department dues calculation and found this liability to be correctly calculated. The actual amount paid was verified to the cash disbursement records.

Federal Income Taxes Payable **$1,329**

This liability represents the balance payable at year-end for federal income taxes incurred prior to December 31, 2004.

The examiners reviewed the company's 2004 tax return and verified amounts paid to cash disbursement records to verify the accuracy of this liability.

Unearned Premiums **$481,277**

This liability represents the reserve established for unearned premiums in compliance with s. Ins 13.08 (3), Wis. Adm. Code. This reserve was established using a daily pro rata methodology.

Reinsurance Payable **$73,470**

This liability consists of amounts due to the company's reinsurer at December 31, 2004, relating to transactions which occurred on or prior to that date.

Class A liability premium	$ 680
Class B first surplus	16,390
Class C C-1 premium	4,450
Class C C-2 premium	2,025
Class D/E premium	9,200
Deferred reinsurance payable	40,725
Total	$73,470

Subsequent cash disbursements, reinsurance accountings, and a WRC letter concerning deferred premiums verified the amount of this liability.

Amounts Withheld for the Account of Others **$5,614**

This liability represents employee payroll deductions in the possession of the company at December 31, 2004. Supporting records and subsequent cash disbursements verified this item.

Payroll Taxes Payable **$1,374**

This liability represents the company's portion of payroll taxes incurred prior to December 31, 2004, which had not yet been paid. Supporting records and subsequent cash disbursements verified this item.

Accounts Payable **$2,191**

This liability represents the president’s salary, miscellaneous utility bills, and office expenses that are payable at year-end 2004. A review of the company’s January 2005 payments showed that this amount was missing the accrual of one week’s payroll that was earned in 2004 but unpaid at year-end. The amount is immaterial so no adjustment to surplus is being made. It is recommended that the company properly accrue for all earned and unpaid payroll amounts in all future annual statements.

Premiums Received in Advance **$19,091**

This liability represents the total premiums received prior to year end for policies with effective dates after December 31, 2004. The examiners reviewed 2004 premium and cash receipt records to verify the accuracy of this liability.

V. CONCLUSION

The company complied with all four of the prior examination recommendations. There were no adjustments or reclassifications to surplus as a result of this examination. There were examination recommendations made concerning properly filing biographical data, directors with conflicts of interest abstaining from voting on matters that involve their conflicts and properly accruing payroll earned but unpaid at year-end.

Surplus, admitted assets, and net premiums earned increased 14.2%, 26.2%, and 42.3%, respectively, over the examination period. Surplus increased between 1999 and 2000 and then decreased in 2001 and 2002 due to years with high net losses and LAE incurred resulting in net losses of $(266,197) in 2001 and $(115,929) in 2002. The company strengthened its underwriting standards and the number of policies in force decreased to 1,403 at year-end 2004. The company’s composite ratio is 87% in 2004, the lowest of the examination period and the company had a net income of $158,911 in 2004, the highest of the examination period.

VI. SUMMARY OF COMMENTS AND RECOMMENDATIONS

1. Page 14 - Corporate Records—It is recommended that the company report biographical data relating to all new officers and directors in accordance with s. Ins 6.52, Wis. Adm. Code.

2. Page 14 - Conflict of Interest—It is recommended that the directors with conflicts of interest properly abstain from voting on matters involving their interest and the minutes clearly indicate such abstentions pursuant to s. 612.18, Wis. Stat.

3. Page 23 - Accounts Payable—It is recommended that the company properly accrue for all earned and unpaid payroll amounts in all future annual statements.

VII. ACKNOWLEDGMENT

The courteous cooperation extended to the examiners by the company's personnel is hereby acknowledged.

In addition to the undersigned, Elena Vetrina of the Office of the Commissioner of Insurance, State of Wisconsin, participated in the examination.

Respectfully submitted,

Kerri Lee Miller
Examiner-in-Charge